UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION

Before Commissioners: Pat Wood, III, Chairman;
William L. Massey, and Nora Mead Brownell.

Northwest Pipeline Corporation Docket No. RP01-416-001

ORDER REJECTING COMPLIANCE FILING

(Issued June 9, 2003)

1. On July 13, 2001, Northwest Pipeline Corporation (Northwest), in response to a Commission order,[1] filed its explanation of why the cost sharing mechanism it has proposed in this proceeding is appropriate only when a shipper elects to pay for lateral facilities under a facility surcharge method of reimbursement, and not when the shipper pays in a lump sum. The Commission does not accept Northwest's explanation and will require Northwest to file revised tariff sheets, as discussed below. This order is in the public interest because it provides for equitable treatment among customers.

Background

2. Section 21 of the General Terms and Conditions of Northwest's tariff sets forth procedures for the construction, operation, ownership, and facilities reimbursement of costs associated with new receipt and delivery facilities that are needed to accommodate customer requests for service. Section 21.3 provides a shipper with two options to reimburse Northwest for the cost of the lateral facilities: (1) under Section 21.3(a), a shipper may reimburse Northwest in full for the actual construction cost of the facilities and related income taxes through a lump sum payment, upon completion of construction; or (2) under Section 21.3(b), a shipper may reimburse Northwest through a surcharge for the cost of service attributable to the facilities.

3. On May 14, 2001, Northwest filed tariff sheets proposing to provide for sharing of lateral facility costs between a shipper for whom a lateral facility was initially constructed and a third-party shipper that has requested service on a relatively inexpensive expansion of the original lateral facility. Specifically, Northwest proposed that if, at the request of a

[1] Northwest Pipeline Corporation, 95 FERC ¶ 61,389 (2001) (June 13 Order).

third-party shipper, Northwest agrees to add or increase compression in order to increase the capacity of lateral facilities currently being paid for by the shipper initially requesting the lateral, then the initial shipper's facility reimbursement charge would be reduced if such shipper's pro rata share of the aggregate rate base of the expanded facilities results in a revised facility reimbursement charge that is less than the initial shipper's current facility reimbursement charge related to those facilities. Northwest's proposal did not address cost sharing for shippers that have elected lump sum reimbursement of lateral costs instead of reimbursement through a facility surcharge. Pan-Alberta Gas Ltd., Pan-Alberta Gas (U.S.), Inc., Mirant Americas Energy Marketing Canada, Ltd., and Mirant Americas Energy Marketing, L.P. (collectively, Pan-Alberta) protested the filing, arguing that the cost sharing option should be available to initial shippers who have chosen the lump sum option. Pan-Alberta argued that such an approach would discriminate unduly against those who opt for the lump sum payment method, and would have the effect of unjustifiably discouraging utilization of that method.

4. In its June 13 Order, the Commission conditionally accepted Northwest's tariff sheets, but directed Northwest to file "an explanation of why cost sharing is only appropriate when a shipper has elected the facility surcharge method of reimbursement instead of the lump-sum payment method.'[2] The Commission's acceptance was further conditioned on the outcome of a pending proceeding in Docket No. RP01-232-001, in which Northwest had proposed to eliminate the lump sum option and to modify its buyout option. However, on July 26, 2001, the Commission rejected Northwest's proposal in that proceeding, on the ground that it would permit Northwest to recover a rate of return for a project in which it has no investment.[3]

5. In the instant filing, Northwest submitted an explanation of why it has proposed a cost-sharing mechanism only when a shipper elects to pay for lateral facilities under a facility surcharge method of reimbursement and not when it elects to pay for facilities on a lump sum basis. Northwest explains that its proposal would provide an equitable sharing of rate base costs between an initial shipper and an expansion shipper in circumstances where cost sharing would result in a lower rolled-in rate to the initial shipper. Northwest asserts that this result would typically occur only if relatively inexpensive compression facilities could be added to an existing lateral.

6. Northwest further explains that the intent of its proposal is to apply the Commission's system expansion rolled-in and incremental rate policy to Northwest's

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[2]95 FERC at 62,453.

[3]Northwest Pipeline Corporation, 96 FERC ¶ 61,128, <u>reh'g denied</u>, 97 FERC ¶ 61,092 (2001).

lateral facilities. If the rolled-in rate would result in a reduction to the initial shipper's facility surcharge, then the total post-expansion rate base would be allocated between the initial and expansion shipper on the basis of contract demand. If the lateral expansion would not produce a lower facility surcharge for the initial shipper, the cost of the expansion would be borne by the expansion shipper.

7. Northwest states that it is not proposing to establish a cost-sharing mechanism for shippers that elect a lump sum method of reimbursement because such a mechanism would be arbitrary, not cost-based, and unduly complex. Northwest explains that, based on its experience, shippers choose the lump sum option for a variety of reasons: (1) the shipper has a lower cost of capital than Northwest; (2) the shipper desires to finance the lateral facilities together with a related industrial or electric generation facility; or (3) the shipper chooses to include the contribution-in-aid of construction in distribution plant rate base. Northwest concludes that it would be unable to calculate a cost-sharing arrangement that is truly cost-based because it is not privy to the economics of these shipper choices. Northwest asserts that, as a result, the initial shipper and the expansion shipper would either be overpaying or underpaying for the service rendered.

8. Northwest further contends that the cost-sharing mechanism would be unduly complex. In its view, tariff provisions would be needed to address a variety of potential business circumstances, including: (a) both the initial shipper and expansion shipper elect the lump sum option; (b) the initial shipper pays on a lump-sum basis but the expansion shipper elects a facility surcharge reimbursement; and (c) the lateral is expanded more than once with varying combinations of (a) and (b). Northwest contends that these possible combinations would result in complex tariff provisions that would be applicable to a very limited universe of transactions.

9. Northwest states that in order to determine whether an expansion is eligible for cost sharing under the rolled-in rate benefit test, one approach would be to determine a cost of service for the existing facilities and the expansion facilities and to compare rates with and without the expansion facilities. According to Northwest, this would involve deciding such issues as what rate design to use (traditional declining rate bases, levelized rates, stated rates, or annual cost of service, etc.); whether a standard rate design method should be used in all circumstances; and what time periods should be used in evaluating the result. In addition, Northwest would need to determine the appropriate depreciation period for the facilities (e.g., the life of the general pipeline system or lateral, the life of the initial shipper's contract or the combination of the initial shipper's contract and the expansion shipper contract).

10. Northwest states that an alternate rolled-in test approach could be used wherein the expansion capital costs could be indexed back to the date that the initial facilities were

constructed. The combined rate base costs could then be split based on the contract demands of the respective shippers.

11. Notice of Northwest's compliance filing was published in the Federal Register, 66 Fed. Reg. 38,658 (2001), with protests due on or before July 26, 2001. Pan-Alberta filed timely comments urging the Commission to reject Northwest's position that it would be too difficult to develop a cost sharing mechanism when the lump sum option is selected, and to direct Northwest to develop "an appropriate and workable cost-sharing approach to apply in those circumstances."[4]

Discussion

12. The Commission finds that it is neither overly complex nor unduly burdensome to develop a cost-sharing mechanism for situations in which the initial shipper elected the lump sum payment option. Furthermore, this option is necessary to ensure that shippers are treated in a non-discriminatory manner and continue to benefit from the flexibility to choose among several financing options.

13. An example of a reasonable approach would be for Northwest to take the depreciated[5] cost of the original lateral, add it to the cost of the expansion, and apportion the costs between the two shippers based on each shipper's contract demand. If the resulting apportioned cost to the second expansion shipper was greater than the expansion cost, that shipper would be responsible for paying the apportioned cost to Northwest. The difference between the apportioned cost and the expansion cost would be credited or refunded by Northwest to the original shipper. This credit or refund could be accomplished two ways. The expansion shipper could make a lump sum payment to Northwest for the credit or refund that Northwest would flow through to the original shipper. Alternatively, Northwest could make the lump sum credit or payment to the original shipper and recover the full apportioned cost from the expansion shipper through a facility surcharge.

14. The Commission therefore directs Northwest to develop a cost-sharing mechanism for shippers who choose the lump sum reimbursement option.

The Commission orders:

(A) Northwest's compliance filing is hereby rejected.

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[4] Pan-Alberta Comments at 2.

[5] Northwest could use the higher of the average depreciation rates underlying the mainline or the contract life of the original shipper's contract.

(B) Northwest is hereby ordered to file within 30 days a proposed tariff revision providing a mechanism for sharing the costs of laterals when a shipper has elected the lump sum payment method.

By the Commission.

(S E A L)

Linda Mitry,
Acting Secretary.